No. 12003

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

THE METROPOLITAN FINANCE CORPORATION OF CALIFORNIA, a corporation,

Appellant,

vs.

ELLSWORTH WOOD and ELAINE SHIPP,

Appellees.

APPELLANT'S BRIEF.

MACFARLANE, SCHAEFER & HAUN,
HENRY SCHAEFER, JR.,
DEXTER D. JONES,
WILLIAM GAMBLE,
1150 Subway Terminal Building, Los Angeles 13,
Attorneys for Appellant.

Parker & Company, Law Printers, Los Angeles. Phone TR. 5206.

TOPICAL INDEX

TABLE OF AUTHORITIES CITED

STATUTES.

TEXTBOOKS

No. 12003

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

THE METROPOLITAN FINANCE CORPORATION OF CALIFORNIA, a corporation,

Appellant,

vs.

ELLSWORTH WOOD and ELAINE SHIPP,

Appellees.

APPELLANT'S BRIEF.

Opinion Below.

Neither the order of the District Court [R. 78-81] nor the Judgment of Dismissal [R. 81-82] is published.

Jurisdiction.

This action was filed by the appellant, a corporation organized and existing under and by virtue of the laws of the State of Delaware, against the appellees, who are all residents and citizens of the State of California. The action is in replevin to recover an automobile over the value of three thousand dollars ($3,000.00). Jurisdiction was acquired by the District Court because of the diversity of citizenship between the appellant and appellees. In accordance with Section 24(1) of the Judicial Code (28 U. S. C. A. Section 41(1)), as it existed at the time of

the filing of the complaint, to wit: April 14, 1948 [R. 2, 3 and 4].

This Court has jurisdiction upon appeal to review the order and the judgment of the District Court under the provisions of Section 128(a) of the Judicial Code, as amended. Title 28, U. S. C. A., Section 225.

Notice of Motion to Dismiss was filed May 7, 1948 [R. 9] and after hearing on June 7, 1948 [R. 85-98] and oral argument being made by both sides [R. 85-98], the Court made its order that the motion of the defendants to dismiss the action be granted [R. 78-81]. Thereafter on the 22nd day of June, 1948, the Court made its Judgment of Dismissal and the same was filed on June 23, 1948 [R. 81-82]. Within the time prescribed by Rule 73 of the Federal Rules of Civil Procedure, Notice of Appeal was filed [R. 82].

Statement.

The Complaint [R. 2-4] states a cause of action against the appellees for claim and delivery under the California Code of Civil Procedure, Sections 509-521. The plaintiff alleged that it was the owner and entitled to the possession of a 1947 Cadillac Sedan of the value of four thousand dollars ($4,000.00); that possession of the said personal property was in the appellees and that they unlawfully claimed the right thereto; that demand had been made of the appellees for possession and the same had been refused. The provisional remedy of claim and delivery under the California statute (Code of Civil Procedure, Sections 509-521), was invoked and the United

States Marshal seized the automobile. After five (5) days, the appellees not having filed a written undertaking with the Marshal as is provided in Section 514 of the Code of Civil Procedure, the Marshal delivered the automobile to the appellant. Thereafter, to wit: on May 4, 1948, the appellee, Ellsworth Wood, filed his answer alleging that he was the owner of the said automobile and entitled to the possession thereof [R. 5-6]. On the same day, to wit: May 4, 1948, the appellee, Elaine Shipp, filed her answer alleging that she was the owner of the said automobile and entitled to the possession thereof [R. 7-9]. On May 17, 1948, there was filed on behalf of the appellees a Notice of Motion to Remand or Dismiss Action [R. 9] and concurrently therewith appellees filed a written Motion to Remand Cause to Superior Court in and for the County of Los Angeles, State of California, or to Dismiss Cause [R. 10-11]. Said motion was based on the grounds that the District Court was without jurisdiction by reason of the fact that appellee, Elaine Shipp, had filed an Answer and Cross-Complaint in an action No. D-356,410 in the Superior Court in and for the County of Los Angeles, State of California, wherein she had alleged that the Cadillac automobile which was the automobile sought to be recovered in this action filed in the District Court, was the community property of Everett S. Shipp and Elaine Shipp, husband and wife, and in said action of the Superior Court, the Court had issued an order restraining and enjoining Everett S. Shipp from interfering with Elaine Shipp's use of the said automobile, and that the action in

the Superior Court was an action *in rem* for the determination of the interest of the husband and wife in the specific *res,* to wit: the Cadillac automobile. That said Superior Court action having been filed prior to the filing of the complaint in the District Court for replevin, the Superior Court in and for the County of Los Angeles, State of California, had prior jurisdiction of the *res,* and the District Court should therefore dismiss the action. That on June 1, 1948, the appellant filed a Statement of Reasons and Opposition to Defendant's Motion to Remand Cause to Superior Court [R. 40-52]. The grounds of the opposition were that the action pending in the Superior Court in and for the County of Los Angeles was between Everett S. Shipp as plaintiff and Elaine Shipp as defendant, and that the appellant, Metropolitan Finance Corporation of California, a Delaware corporation, was not a party to that action and that as between Metropolitan Finance Corporation of California as plaintiff and Ellsworth Wood and Elaine Shipp as defendants, the District Court of the United States had jurisdiction to determine the title to the property which is the subject of this action. That on June 7, 1948, the matter was argued before the Honorable William C. Mathes [R. 85-98] and on June 17, 1948, the Honorable William C. Mathes made his Order on Motion of Defendants to Dismiss the Action [R. 78-81]. Said order was based on the grounds that the District Court lacked jurisdiction of the subject matter of the action and pursuant to said order on motion, a Judgment of Dismissal was entered June 23, 1948 [R. 81].

Question Presented.

Whether the Federal District Court can properly dismiss an action of which it has jurisdiction of the parties and the subject matter, against a party seeking to recover the possession of an automobile on the grounds that a prior action in the State Court has been commenced involving the same property, when the State Court action is an action for divorce and for division of community property, and the plaintiff in the action in the Federal Court is not a party to the action in the State Court, and said plaintiff claims that the said automobile was at all times the property of said plaintiff, Metropolitan Finance Corporation of California and was at all times entitled to the possession thereof.

Summary of Argument.

The Cross-Complaint filed by Mrs. Shipp in the Superior Court of California in and for the County of Los Angeles [R. 20-26], in which she alleged the property here in question to be the community property of the spouses and as to which an injunction was issued [R. 27], did not give the said Superior Court exclusive jurisdiction over such property. The jurisdiction of the State Court in an action for divorce extends only to the separate property of the spouses or to the community property. There is no jurisdiction in such Court over the property of third persons not made a party to the divorce action. Thus, in this instance the only property over which it is possible that the State Court had achieved "constructive

possession" is the property that belonged to the spouses or either of them and as to which issues were raised by the pleadings. Without an allegation that the third party has an interest in the property, the State Court cannot act in regard to such property so as to defeat the rights of the third party.

In order for the jurisdiction of the State Court to be exclusive it must be shown that the action in the Federal Court will interfere with the State Court's possession of the property, such possesion being essential to the action in the State Court. Possession of the property is not essential to "divide" the interests of the spouses in property alleged to be community property. In this action judgment by the Federal Court would not interfere with the action in the State Court which is for a "division" of the community property and not for a recovery of possession of such property.

There having been no issue of the corporate entity raised in the Superior Court and no allegation of fraud in the Federal Court the plaintiff herein must be regarded as a separate entity and not as the *alter ego* of Mr. Shipp.

ARGUMENT.

I.

The State Court in a Divorce Action Does Not Acquire Exclusive Jurisdiction Over Property of the Spouses Which Would Preclude the Federal Court From Determining Rights Therein Claimed by Third Parties Not Joined in the State Court.

In order to determine whether the District Court properly dismissed the action of the appellant, it is necessary to inquire into the nature of the jurisdiction of the Superior Court of the State of California in an action for divorce in which the appellee, Elaine Shipp, was a party defendant and who in the allegation of her Answer and Cross-Complaint alleged that the property which is the subject of the present action was the community property of herself and Everett S. Shipp. In the divorce action no parties were joined other than the husband and wife as plaintiff and defendant, respectively. Neither the appellant, Metropolitan Finance Corporation of California nor appellee Ellsworth Wood were joined as parties in said action and did not intervene therein. Everett S. Shipp, the plaintiff and cross-defendant in the divorce action was not and has never been a party to the proceeding before the District Court.

It is undoubtedly true that an action for divorce, in so far as it relates to the status of the parties, is an action *in rem,* the marital relation being considered as the *res.*

DeLaMontanya v. DeLaMontanya, 112 Cal. 101, 44 Pac. 345 (1896);

Estate of Lee, 200 Cal. 310, 253 Pac. 145 (1927);

Borg v. Borg, 25 Cal. App. 2d 25, 76 P. 2d 218 (1938).

It is clear from an analysis of these cases that an action for divorce cannot be classified purely as an action *in rem*. Thus in so far as the action relates to such matters as alimony, costs and attorney's fees it is strictly an action *in personam*.

Matter of McMullin, 164 Cal. 504, 129 Pac. 773 (1912);

DeLaMontanya v. DeLaMontanya, 112 Cal. 101, 44 Pac. 345 (1896) .

The limitation of the jurisdiction of the State Court in a divorce action with respect to property is to determine the status of such property either as community property or as separate property of one of the spouses. Such an action has not been declared to be an action *in rem* and the courts have declared that the determination of the status of property as between the spouses in a divorce action can in no way affect the interest of third parties in such property.

Cummings v. Cummings, 75 Cal. 434, 17 Pac. 442 (1888);

Elms v. Elms, 4 Cal. 2d 681, 52 P. 2d 223 (1935);

Callnon v. Callnon, 7 Cal. App. 2d 676, 46 P. 2d 988 (1935).

In the case of *Cummings v. Cummings,* 75 Cal. 434, 17 Pac. 442 (1888), the trial court, in an action for divorce, partitioned certain real property held to be community property of the spouses which was in the possession of a

third party mortgagee. In decreeing a partition of the property, the trial court held that the mortgagee could look to the wife's share for only one-half of the mortgage debt. The Supreme Court reversed said judgment and stated that the trial court was not justified in attempting to limit or change the liabilities created by the mortgage or in altering in any way the mortgagee's rights or the obligations of the community under the contract. It may be further noted that the decision of the court expressly limited the plaintiff to relief consistent with the complaint. In the divorce action between appellee Elaine Shipp and her husband, there was no issue framed as to the ownership of the automobile except as between the spouses.

In *Callnon v. Callnon,* 7 Cal. App. 2d 676, 46 P. 2d 988 (1935), the court pointed out that in a divorce action jurisdiction as to property is obtained only over the rights of parties who are before the court in the case. At page 681 the court states:

> "From the foregoing, and from the authorities which we will hereafter cite, it may be taken as settled that the jurisdiction of the court in a divorce proceeding over property rights is limited to the property which belongs to the community or which is the separate property of the spouses. This jurisdiction is found in sections 141 *et seq.* of the Civil Code which authorize the *division* of the community property and a lien upon the separate property of the husband in aid of the enforcement of remedial orders made in the proceeding. . . . Hence, unless the pleadings in divorce allege that a third party claims

an interest in the community property or holds separate property in fraud of one of the spouses, the court is without jurisdiction in the divorce proceeding to determine the property rights of the third party."

The District Court in the instant case states in its order to dismiss the action [R. 78-79] that the proceedings for divorce give the Court jurisdiction to hear and determine matters relating to the status of property alleged to be community property and that the Court necessarily assumes control of the property in controversy. Citing *Huber v. Huber,* 27 Cal. 2d 784, 167 P. 2d 708 (1946); *Salveter v. Salveter,* 206 Cal. 657, 275 Pac. 801 (1929).

Both of these cases relate to the power of the court in an action for divorce to declare the status of the property whether community or separate as between the spouses. Neither of these cases, however, can be cited as authority for the proposition that the court assumes control of the property except for the limited purpose of determining the respective interests of the parties.

In *Salveter v. Salveter,* 206 Cal. 657, 275 Pac. 801 (1929), at 660, the court states:

"In an action for divorce between two discordant spouses the trial court, upon proper averments and under the express provisions of those sections of the Civil Code (secs. 82-148), regulating actions for divorce, *is invested with full power to determine the status of the property of both or each of the spouses,* regardless of the name of either in which the title to such property stands, * * *" (Emphasis added.)

It can readily be seen that there was no question as to the powers of the court other than as they related to the parties before the court.

In this action the automobile was registered in the name of the plaintiff, Metropolitan Finance Corporation, as both legal and registered owner. This plaintiff was not made a party to the divorce action. Inasmuch as the divorce court was limited in its jurisdiction to determine the rights of the parties then before it for the purpose of declaring their community or separate interests in said property and as such declaration could not affect the rights of any person not joined in said action, it is difficult to see wherein the divorce court had assumed such control of the property as would prevent this court or any other court from determining the title, interest or possession of said property in a party not joined in the divorce action. It is clear from the cases cited that the jurisdiction of the divorce court over the property of the spouses is a very limited jurisdiction for the purpose only of determining the rights and obligations of the community in such property and the court cannot deprive a third party from seeking a determination of his property rights in a second action.

II.

In an Action for Divorce the Court Does Not Acquire Such Possession or Control of the Property as to Divest a Federal Court From Determining Rights With Respect Thereto Involving Parties Not Joined in the Divorce Action.

In an action for divorce possession by the State court in order to "divide" the community property is not essential. This is illustrated by the fact that the rights of a third party who was not made a party to the action are not affected by the decree of the divorce court. The court can decree the interest, if any, of the spouses in the property without the necessity of possession.

> *Cummings v. Cummings,* 75 Cal. 434, 17 Pac. 442 (1888).

The mere filing of the action for divorce does not bring the property of the parties into the custody of the court.

> *Lord v. Hough,* 43 Cal. 581 (1872);
>
> *Sun Insurance Company v. White,* 123 Cal. 196, 55 Pac. 902 (1898).

Lord v. Hough at page 585, and quoted in *Sun Insurance Company v. White* at page 200, states:

> "The pendency of proceedings for divorce does not of itself interrupt the exercise of the husband's powers. The property does not come into the custody of the court by the institution of the suit. The husband has still the control of it, and full power of disposition of it. He is held to equal good faith in all transactions relating to it as before the commencement of the suit. He is subject to the same restrictions in its disposal. He cannot make a voluntary conveyance of any portion of the property, with the

intent to deprive the wife of her claim in anticipation of divorce, any more than he could make such fraudulent disposition in anticipation of her widowhood."

Nor does the issuance of an injunction against the husband to prevent his interference with the use of the property by the wife have the effect of drawing the property into the custody of the court. It is the rule in California that an injunction operates strictly *in personam.*

Berger v. Superior Court, 175 Cal. 719, 167 Pac. 143, 15 A. L. R. 373 (1917).

Further, a court in a divorce proceeding has jurisdiction to adjudicate and dispose of the property rights of the parties in real property outside of the jurisdiction of the court where such property was put in issue by the pleadings.

Spahn v. Spahn, 70 Cal. App. 2d 791, 152 Pac. 253 (1945).

It is clear that if possession were necessary for the State court to give an effective decree as to the status of the property it could give no decree effecting the status of foreign real property.

In order to divest a Federal Court of jurisdiction to determine the matter presented in this controversy it must be shown that the action in the Federal Court will interfere with the possession of the property of the State court and that such possession in the State court was essential to the effective disposition of that court's action. Conflict of jurisdiction as to the subject matter of the litigation which would defeat a second action over the same subject matter does not mean merely that the two suits relate to the same physical property or that either court had actual

or constructive possession thereof. It means that the issues involved, relief prayed for and the parties to the two suits are "so substantially alike that *lis pendens* of the last brought is included in the first."

Empire Trust Co. v. Brooks, 232 Fed. 641 at page 648 (1916).

Throughout the cases relating to conflicting jurisdiction of State and Federal Court it is clear that in order to have the State court action bar the Federal action, possession of the subject matter in the State court must be maintained by that Court only where such is essential to give effect to their judgment.

McClellan v. Carland, 217 U. S. 268, 30 S. Ct. 501, 54 L. Ed. 762 (1909);

Pacific Live Stock Company v. Lewis, 241 U. S. 440 (1915), 60 L. Ed. 1084;

Harkin v. Brundage, 276 U. S. 36, 48 S. Ct. 268, 72 L. Ed. 457 (1928);

Empire Trust Co. v. Brooks, 232 Fed. 641 (1916);

Boynton v. Moffat Tunnel Improvement District, 57 F. 2d 772.

In the last cited case at page 779, it is stated:

"The rule that as between two actions *quasi in rem* the one first filed excludes the latter one is *subject to an important and well settled qualification, to wit, that the two actions shall invoke the same jurisdiction.* This qualification is essential to the administration of justice; except for it, a stockholder could apply for a receiver and either indefinitely postpone relief to creditors or bond holders, or could require them to come to the court of the stockholder's selection." (Emphasis added.)

If the filing of an action for divorce in which an injunction is issued against a husband preventing his interference with the wife's possession of certain properties were sufficient to bar all subsequent actions by persons not made a party to the divorce action, it would seem that a party to the divorce action could effectively tie up property of any third party whether the community had an interest in said property or not. Thus the effect of the dismissal by the District Court is to require the appellant to withhold any action for the possession of its property until a final determination has been made of the property rights in the divorce action. It is difficult to see any distinction between the instant case and that in which a piece of realty is purchased by a third party holding the legal title and in which neither the husband nor wife had an interest except that the wife held possession adversely. In this example the true owner would surely not be barred from bringing an action for ejectment until after the spouses had settled their marital differences. The nature of the two actions is entirely different in purpose and does not conflict.

The case of *Harkin v. Brundage* (276 U. S. 36, 48 S. Ct. 268, 72 L. Ed. 457 (1928)), emphasizes the point that where there is a great difference in the nature of the actions brought, there is no conflict between two jurisdictions. In that case, the Federal Court appointed a receiver in an action brought by a creditor. Prior to the filing of the bill in the Federal Court, a stockholder had filed a bill in a State Court for a receiver of the same property. Both actions were *quasi in rem* and in both cases control over the same property was necessary to effectuate any later decree. The Circuit Court of Appeals held that the two actions were so different that the Federal Court could proceed irrespective of the pendency of the State

action. Although the Supreme Court reversed the case, on other grounds, it held that the Circuit Court was correct in its holding in this respect.

The District Court in its order to dismiss [R. 78-81], relies upon the cases of *Princess Lida v. Thompson,* 305 U. S. 456 (1939); *U. S. v. Bank of N. Y. & Trust Co.,* 296 U. S. 463 (1936) and *Penn General Casualty Co. v. Penn.,* 294 U. S. 189 (1935). Those cases also recognize the proposition that the second suit is barred only where possession is necessary in the State Court and where the two suits have substantially the same purpose. Thus in *Pennsylvania General Casualty Co. v. Pennsylvania,* 294 U. S. 189, 79 L. Ed. 850 (1935), pages 855-856, it is stated:

> "But if the two suits are *in rem* or *quasi in rem requiring* that the court or its officer have possession or control of the property which is the subject of the suit in order to proceed with the cause and to grant the relief sought, the jurisdiction of one court must of necessity yield to that of the other. * * * If the two suits do not have substantially the same purpose, and thus the jurisdiction of the two courts may not be said to be strictly concurrent, and if neither court can act effectively without acquiring possession and control of the property *pendente lite,* the time of acquiring actual possession may perhaps be the decisive factor." (Emphasis added.)

The jurisdiction of the divorce court being limited to a determination of the property rights as between the parties before that court and the decree of the court with respect to the property acting only upon the interest of those parties and possession of the property by the court not being essential to effectuate its decree, the Federal Court

cannot properly divest itself of jurisdiction to hear and determine any rights with respect to such property when the issues delineated by the pleadings and the parties before the court are in all essential respects different from those presented in the divorce action.

III.

A Corporate Entity Will Be Disregarded Only Where the Facts Disclose It Is Necessary to Prevent Fraud.

The District Court upon the hearing for the motion to dismiss indicated that it was not favorably inclined to resolve the fiction with respect to corporate entity to permit a corporation doing the greater portion of its business within a State to come into the Federal Court on the basis of diversity of citizenship and to obtain the benefits allowed such corporation in the Federal Court [R. 97]. It is apparent therefore, that the District Court must have determined in granting the motion to dismiss that the appellant was not in fact a separate corporate entity but was the *alter ego* of one of its stockholders, Mr. Everett S. Shipp. If it were not the express intention of the court so to hold, the basis of the judgment of dismissal is not well founded in law as shown in points I and II of this brief.

It is a long settled rule that a corporation is regarded as a separate and distinct entity from the stockholders comprising the corporation. This is true even though the stock is all owned by one or two parties. The separate

entity of the corporation is deemed a citizen of the State of its incorporation.

Doctor v. Harrington, 196 U. S. 579, 49 L. Ed. 606, 25 S. Ct. 355 (1904);

Louisville C. & C. R. Co. v. Letson, 2 How. (U. S. 497, 11 L. Ed. 353 (1844).

A corporation as a distinct entity may be disregarded in a diversity of citizenship case only where the corporation was formed for the sole purpose of collusively attaining Federal jurisdiction.

Miller & Lux v. East Side Canal & Irrigation Co., 211 U. S. 293, 53 L. Ed. 189, 29 S. Ct. 111 (1908).

In the present case there has been no attempt made to show that the jurisdiction here invoked by the plaintiff was collusive in nature.

The only other bases for disregarding the corporate entity are where the facts show that it is necessary to disregard the entity in order to prevent fraud, protect the rights of third persons or prevent a palpable injustice.

In re Sterling, 97 F. 2d 505 (1938);

Majestic Company v. Orpheum Circuit, 21 F. 2d 720, 722 (1927);

Wenban Estate v. Hewlett, 193 Cal. 675, 227 Pac. 723 (1924);

Minifie v. Rowley, 187 Cal. 481, 202 Pac. 673 (1921).

Citing the two last cited California cases, Mr. Fletcher in *I Cyclopedia of the Law of Corporations,* at page 142, states:

> "Whether the corporation shall be disregarded depends on questions of fact, to be appropriately pleaded, and the presumptions are that the stockholders or officers and the corporation are distinct entities."

In the present case the only allegations in the answers of defendants Ellsworth Wood [R. 5-6] and Elaine Shipp [R. 7-8], in regard to the identity of Mr. Shipp and the plaintiff corporation are that Mr. Shipp owns "at least 85% of the stock of the Metropolitan Finance Corporation of California, a corporation" and that title to the property was taken in the plaintiff corporation for tax purposes. These allegations at most would indicate that Mr. Shipp had a large and controlling interest in the corporation. Whether he is the sole stockholder or there are many stockholders is not the controlling factor as to whether or not a corporate entity should be disregarded.

Majestic Company v. Orpheum Circuit, 21 F. 2d 720, 722 (1927);

Erkenbrecher v. Grant, 187 Cal. 7, 200 Pac. 641 (1927).

There is no allegation in the answer nor in the affidavit set forth on the motion to dismiss which alleges that any fraud or injustice would be imposed upon any party to this action should the corporate entity not be disregarded. The only purpose for disregarding the corporate entity was to divest the Federal Court of jurisdiction to hear and determine this matter. As has been shown by the decisions with respect to this proposition of law the corporate entity

will not be disregarded unless upon a proper showing of facts upon a trial of the merits of the cause it is shown that to indulge in the corporate fiction would be prejudicial to the interest of one of the parties to such an extent as to amount to fraud or a palpable injustice.

Conclusion.

The judgment of dismissal should be reversed and the case remanded to the District Court for trial on the merits.

Respectfully submitted,

MACFARLANE, SCHAEFER & HAUN,
HENRY SCHAEFER, JR.,
DEXTER D. JONES,
WILLIAM GAMBLE,
By WIILIAM GAMBLE,
Attorneys for Appellant.